

UNITED STATES OF AMERICA
SMALL BUSINESS ADMINISTRATION
OFFICE OF HEARINGS AND APPEALS
WASHINGTON, D.C.

IN THE MATTER OF:

COLAMCO, Inc.

Petitioner

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Docket No. SDB-2006-08-08-04

Decided: October 20, 2006

APPEARANCES

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DIGEST

The Small Disadvantaged Business (SDB) certification, and recertification, process provides an impartial evaluation of the applicant's qualifications and grants due process rights required for fundamental fairness. In accordance with 13 C.F.R. § 124.1008(f)(3)(i), an applicant may respond to issues raised by the Small Business Administration (SBA) in an initial denial of an SDB application by requesting reconsideration. Moreover, if the applicant is denied certification on reconsideration solely on issues not identified in the initial denial, the applicant can request reconsideration and is afforded all the rights available as if it is an initial denial. 13 C.F.R. § 124.1008(f)(3)(ii).

REMANDING PROCEEDING

HOLLEMAN, Administrative Judge:

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Jurisdiction

This appeal petition is decided under the Small Business Act of 1958, 15 U.S.C. § 631 *et seq.*, and 13 C.F.R. Parts 124 and 134.

Issue

Whether SBA declined the application of Colamco, Inc. (Petitioner) on reconsideration solely on issues not raised in the initial denial and denied Petitioner the opportunity to respond to the SBA's new reason for denial on reconsideration. 13 C.F.R. §124.1008(f)(3)(ii).

I. BACKGROUND

A. The Application for Certification

Petitioner was first certified under the Small Business Administration (SBA) Small Disadvantaged Business (SDB) program in 1999 and Petitioner was recertified in 2002. In 2005, Petitioner filed another application for recertification. Petitioner's claim of eligibility is based upon Mr. Juan G. Saldarriaga, Petitioner's president and majority shareholder. Mr. Saldarriaga is a Hispanic American and, thus, is presumed to be a socially disadvantaged individual.

B. The Initial Denial of Petitioner's Application for Certification

On October 31, 2005, the Assistant Administrator of the Division of Program Certification and Eligibility of SBA's Office of Business Development (AA/DPCE) denied Petitioner's application because she concluded the individual upon whom Petitioner's eligibility is based, Mr. Saldarriaga, is not economically disadvantaged. The AA/DPCE found that Mr. Saldarriaga's average Adjusted Gross Income (AGI) for the past two years totals \$614,516, exceeding the AGI of the top 2% of all taxpayers for 2002 according to Internal Revenue Service (IRS) tables, and therefore, Mr. Saldarriaga fails to qualify as an economically disadvantaged individual.

The AA/DPCE informed Mr. Saldarriaga he may request reconsideration of the decline decision within 45 days. In addition to requesting reconsideration, the AA/DPCE also informed Mr. Saldarriaga he may appeal the decision directly to SBA's Office of Hearings and Appeals (OHA).

C. Reconsideration of Petitioner's Application

On December 2, 2005, Petitioner requested reconsideration of its SDB application for certification. Petitioner asserted that the AA/DPCE incorrectly computed Mr. Saldarriaga's income. Petitioner asserted it is a subchapter S corporation. Petitioner further asserted SBA has determined that undistributed subchapter S corporation taxable income reported on an individual's return should be excluded from that individual's income for purposes of determining

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disadvantaged status. Petitioner asserts that SBA Standard Operating Procedure (SOP) 80 05 3 8(a) Program, Chapter 2D, ¶ 5.b (July 20, 2004) provides for the exclusion of any portion of an individual's S corporation income reinvested into the corporation from their own AGI.

Petitioner asserted it had taxable income in 2003 and 2004 but did not distribute any to Mr. Saldarriaga, but accumulated it in retained earnings. Petitioner asserted this S corporation income should be excluded from Mr. Saldarriaga's income. Petitioner further asserted that Mr. Saldarriaga's spouse's income should be excluded from Mr. Saldarriaga's income. Petitioner stated that with these exclusions, Mr. Saldarriaga's average AGI is \$161,141 and is well below the top 2% threshold of all AGI's.

D. The Second Denial of Petitioner's Application

On June 23, 2006, the Acting AA/DPCE (AAA/DPCE) denied Petitioner's request for reconsideration. The AAA/DPCE reviewed Petitioner's request and concluded that Mr. Saldarriaga was not economically disadvantaged based on an average two-year AGI for 2003 and 2004 of \$384,390. The AAA/DPCE noted this income exceeded the top 1% threshold of all taxpayers for the year 2003.

The AAA/DPCE arrived at a two-year average AGI of \$384,390 by taking the sum of Mr. Saldarriaga's AGI from his individual tax form filed in 2003 and 2004, and subtracting from it S corporation income reinvested into Petitioner during those two years, subtracting Mr. Saldarriaga's spouse's income, subtracting income taxes paid by Mr. Saldarriaga on Petitioner's income, and adding K-1 distributions received by Mr. Saldarriaga from Petitioner. The AAA/DPCE did deduct taxes paid on behalf of Petitioner, but did not deduct Mr. Saldarriaga's personal income tax. Further, the AAA/DPCE found that money distributed to Mr. Saldarriaga from Petitioner must be counted as part of Mr. Saldarriaga's income when he received it, even if it was not earned in 2003 and 2004.

The AAA/DPCE informed Mr. Saldarriaga he may appeal the decision of the AAA/DPCE denying his business's application following reconsideration to SBA's OHA.

E. The Appeal Petition

On August 7, 2006, Petitioner filed the instant Appeal Petition seeking to reverse the AAA/DPCE's decision. Petitioner alleges the AAA/DPCE erroneously concluded that Petitioner's president and majority shareholder, Mr. Saldarriaga, was not economically disadvantaged.

Petitioner argues SBA must use an individual's AGI as the starting point for determining personal income. Petitioner further argues there are certain regulatory exclusions from AGI. Petitioner asserts the SOP requires SBA to exclude any portion of an individual's income used to pay S corporation taxes from his or her AGI. Further, that the SOP excludes any portion of S corporation income reinvested into the corporation. SOP, Ch. 2D, ¶ 5.b(2).

Petitioner argues OHA's precedent, while it has allowed exclusions from AGI, has never allowed additions to the AGI. Petitioner argues, despite precedent, the AAA/DPCE has made additions to the AGI, by counting K-1 distributions to Mr. Saldarriaga. These distributions represent previously taxed but undistributed taxable income for Mr. Saldarriaga. Petitioner argues these distributions represent income which Petitioner made and reported to the IRS and paid taxes upon in previous years. According to Petitioner, the K-1 distributions represent income which SBA has already counted as income for Mr. Saldarriaga when certifying and recertifying Petitioner in 1999 and 2002.

Petitioner asserts by adding the K-1 distributions to an individual's AGI, it becomes a modified AGI. Petitioner argues OHA's precedent does not permit SBA to modify an AGI when determining economic disadvantage.

Thus, Petitioner argues the AAA/DPCE's decision is arbitrary, capricious, and contrary to law not only because it departs from SBA's established practice, but also because it departs from this Office's established precedent which has not permitted the Agency to add any additional amounts to an individual's AGI. According to the Petitioner, it results in double counting income Petitioner earned in previous years when it was certified and recertified.

F. SBA's Response

On September 21, 2006, SBA filed the Agency Response to the Appeal Petition. SBA asserts it properly determined Petitioner was not economically disadvantaged based on Mr. Saldarriaga's income. SBA argues an individual's AGI is the starting point for determining an individual's personal income. SBA asserts all personal income, from whatever source, is considered in determining economic disadvantage. Although SBA starts with the AGI, it must consider all other income actually received by an individual in a given year. SBA is not determining taxable income, but assessing all income received by the individual in a particular year. SBA asserts it may properly consider as personal income the distributions from an S corporation.

SBA asserts Petitioner is mistaken when it asserts SBA is double counting Mr. Saldarriaga's income. SBA excludes the amount of S corporation income actually used to pay taxes or reinvested in the applicant concern. The K-1 distributions received were derived from income reinvested by Mr. Saldarriaga in Petitioner. That is, income previously taxed by the IRS, and not counted against Mr. Saldarriaga's income by SBA when it calculated his personal income in the previous certifications. Accordingly, SBA argues these distributions are properly included when determining Mr. Saldarriaga's income since the distributions are received as income and not previously counted as part of his income.

SBA asserts when it computed Mr. Saldarriaga's income, it found he was in the top 1% of all taxpayers, according to IRS tables. SBA further asserts Mr. Saldarriaga would be in the top 1% even if all of his S corporation income and distributions were excluded. Therefore, SBA

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argues the AAA/DPCE found Mr. Saldarriaga was not economically disadvantaged and denied Petitioner's application for recertification.

G. Petitioner's Reply to SBA's Response

On October 2, 2006, Petitioner replied to the SBA's response. Petitioner reiterates SBA should not have counted distributions to Mr. Saldarriaga as additional income for the years 2003 and 2004 when the distributions are from previously reported and taxed income. Petitioner asserts adding the distributions amounts to an inappropriate alteration of Mr. Saldarriaga's AGI.

Petitioner argues SBA has not responded to Petitioner's contention that SBA improperly modified Mr. Saldarriaga's AGI by adding back distributions that were reported as income in previous years. Additionally, Petitioner asserts SBA has effectively counted the same income for two different certifications and SBA's arguments to the contrary are not supported by the evidence. Petitioner reiterates its contention SBA's recertification denial was arbitrary, capricious, and contrary to law. Petitioner also attached a sworn affidavit of Mr. Saldarriaga and a breakdown of Petitioner's retained earnings.

On October 4, 2006, Petitioner filed a Motion for Leave to File Attachments. The attachments were referred to in the in Mr. Saldarriaga's sworn affidavit and included Petitioner's tax information, as well as an additional copy of Mr. Saldarriaga's sworn statement and a copy of the breakdown of Petitioner's retained earnings. Also, on October 4, 2006, Petitioner moved to correct errors in its original reply to SBA's Response.

On October 19, 2006, SBA filed a Response to Petitioner's Reply. SBA argues that Petitioner's own calculations place Mr. Saldarriaga in the top percentile of U.S. incomes.

II. DISCUSSION

A. Timeliness

Petitioner's Appeal Petition, filed within 45 days after the SBA served its decision denying SDB certification, is timely. 13 C.F.R. § 134.202(a)(1).

B. SBA's Claim of Privilege

The SBA submits a claim of deliberative process privilege as to the Business Opportunity Specialist's analysis of Petitioner's initial application, and Petitioner's request for reconsideration. The SBA submits a claim of attorney-client privilege as to the legal opinions on Petitioner's application and request for reconsideration and the communications between counsel and SBA officials. Petitioner did not object to SBA's claim of privilege. After an *in camera* inspection of the documents, I find they fall within the claimed privileges. These documents are internal predecisional memoranda embodying the analysis and recommendations of agency officials to the AAA/DPCE, and thus protected under the deliberative process privilege to protect

the agency's decision-making process. *NLRB v. Sears, Roebuck & Co.*, 421 U.S. 132, 150-152 (1975); *Matter of Henze Industries*, SBA No. SDBA-111, at 7-9 (1999). The legal opinion is also protected under the attorney-client privilege. *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981); *Henze Industries*, SBA No. SDBA-111, at 7-9. SBA's claim of privilege is GRANTED.

C. The Standard of Review

In considering an appeal petition, OHA reviews the AAA/DPCE's determination. OHA's standard of review is whether the record demonstrates the determination was "arbitrary, capricious, or contrary to law." 13 C.F.R. § 124.1008(f)(4)(ii). The scope of review under the "arbitrary and capricious" standard is narrow and OHA cannot substitute its judgment for that of the AAA/DPCE.¹ *Matter of Aero CNC, Inc.*, SBA No. SDBA-106, at 7 (1999). OHA must consider whether the AAA/DPCE's decision "'was based on a consideration of the relevant factors and whether there has been a clear error of judgment.'" *Matter of IRECOR, Inc.*, SBA No. SDBA-104, at 5 (1999) (citing *Bowman Transportation, Inc. v. Arkansas-Best Freight System, Inc.*, 419 U.S. 281 (1974)).

In determining whether the applicant business has met its burden (13 C.F.R. § 124.1008(c)(2)), the AAA/DPCE must examine the relevant data and articulate a satisfactory explanation for its action, including a "'rational connection between the facts found and the choice made.'" *IRECOR*, SBA No. SDBA-104, at 5 (citing *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983)).

On appeal, an applicant for SDB certification has the burden of demonstrating that socially and economically disadvantaged individuals own and control the business. 13 C.F.R. § 124.1008(c)(2). SBA has detailed the ownership and control requirements in 13 C.F.R. §§ 124.105 and 124.106.²

D. Economic Disadvantage

In order to be eligible for certification as an SDB, a business concern must be a small business "owned and controlled by socially and economically disadvantaged individuals." 13 C.F.R. § 124.1001(b); *see also* 13 C.F.R. § 124.101. The business must qualify as small under the applicable size standard, *see* 13 C.F.R. Part 121, be at least 51% owned and controlled by socially and economically disadvantaged individuals, and have its management and daily business operations owned and controlled by one or more socially and economically disadvantaged individuals. 13 C.F.R. § 124.1002(b).

¹ The regulation refers to the official who handles SDB eligibility determinations as the Assistant Administrator for Small Disadvantaged Business Certification and Eligibility (AA/SDBCE). 13 C.F.R. § 124.1008(a). This task is currently performed by the AAA/DPCE.

² The SDB program has adopted the 8(a) eligibility criteria. 13 C.F.R. § 124.1002(a); *Matter of Trisha Koch & Associates*, SBA No. SDBA-113, at 4 (1999).

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Socially disadvantaged individuals are persons who have been subjected to racial or ethnic prejudice or cultural bias within American society because of their identities as members of groups and without regard to their individual qualities. 13 C.F.R. § 124.103(a). Here, SBA does not dispute that Mr. Saldarriaga is a socially disadvantaged individual and that he controls the business, the issue is whether Mr. Saldarriaga is economically disadvantaged.

Economically disadvantaged individuals are socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities as compared to others in the same or similar line of business who are not socially disadvantaged. 13 C.F.R. § 124.104(a). In considering whether an individual has experienced diminished capital and credit opportunities, SBA will examine the individual's personal income for the last two years, personal net worth, the fair market value of all assets, whether encumbered or not, and the financial condition of the applicant compared to the financial profiles of small businesses in the same or similar industry. 13 C.F.R. § 124.104(c).

The AAA/DPCE examined Mr. Saldarriaga's income tax returns and compared them to the IRS tables for the relevant tax years. Based on this comparison SBA argues Mr. Saldarriaga's AGI for the past two years is securely within the top 1% of all incomes in the nation. OHA's precedent has long held once SBA has established the individual upon whom an applicant business's claim of eligibility is based has an AGI in the top 2%, the individual is not economically disadvantaged. *Matter of Tec-Masters, Inc.*, SBA No. SDBA-167, at 7 and n. 3 (2006) (applicant owner ineligible for SDB program because his AGI placed him in top 2% of all taxpayers). Further, establishing this one factor alone is enough to support a finding that an individual is not economically disadvantaged. *Id.*

Petitioner contends SBA miscalculated Mr. Saldarriaga's income by improperly adding Petitioner's K-1 distributions. Petitioner states the distributions received by Mr. Saldarriaga in 2003 and 2004 were not counted as additional income by the IRS because the distributions were reported and taxed prior to 2003. Further, Petitioner argues SBA considered the amounts in Petitioner's 2002 recertification. SBA contends there is a distinction between income for the purpose of SDB certification and for the purpose of taxation by the IRS.

SBA is correct that AGI serves a different role in SBA's certification process as compared to the function for the IRS. However, SBA overlooks the longstanding policy of not manipulating an applicant owner's AGI when calculating personal income to determine a socially disadvantaged individual's economic status. One of the reasons SBA relies on an applicant owner's AGI is to gauge the applicant owner's AGI compared to taxpayers nationwide. If the applicant owner's AGI places him in the top two percent of taxpayers nationwide SBA has consistently found the owner is not economically disadvantaged.³ Yet, comparing an applicant

³ This Office's precedent has repeatedly affirmed once SBA establishes the socially disadvantaged applicant owner's AGI is in the top percentile of all taxpayers nationwide, the applicant owner is not economically disadvantaged. *See Matter of Tec-Masters, Inc.*, SBA No. SDBA- 167 (2006) (owner with two-year average AGI of \$262,397, placing him in the top

owner's AGI to the AGIs of all taxpayers loses its utility if the SBA manipulates the owner's AGI by adding or subtracting amounts. Moreover, manipulating an individual's AGI, with limited exceptions (such as excluding the income attributable to a spouse in a joint return, *see Matter of Oak Ridge Tool-Engineering, Inc.*, SBA No. SDBA-136 (2000)), has not been permitted. *See Matter of C & S Paving, Inc.*, SBA No. BDP-231 (2006) (rejecting attempt to reduce petitioner's disadvantaged owner's AGI through consideration of gambling losses); *Matter of Tower Communications*, SBA No. MSB-587 (1997) (holding SBA's determination denying 8(a) program entry to petitioner was arbitrary, capricious, and contrary to law when SBA modified petitioner's owner's AGI by adding net operating loss carryovers).

E. Due Process

The SDB certification, and recertification, process is devised to provide an impartial evaluation of the applicant's qualifications and to grant due process rights required for fundamental fairness. In accordance with 13 C.F.R. § 124.1008(f)(3)(i), an applicant may respond to issues raised by SBA in an initial denial of an SDB application by requesting reconsideration. Moreover, if the applicant is denied on reconsideration solely on issues not identified in the initial decline, the applicant can request reconsideration and is afforded all the rights available as if it is an initial denial. 13 C.F.R. § 124.1008(f)(3)(ii).

In its initial denial, on October 15, 2005, SBA concluded Mr. Saldarriaga is not economically disadvantaged because Mr. Saldarriaga's average AGI for the past two years totaled \$614,516. Although SBA did not indicate how Mr. Saldarriaga's two-year average AGI was calculated, it is obvious SBA used a simple calculation based on an average of Mr. Saldarriaga's 2004 AGI, \$567,271, and his 2003 AGI, \$661,761. Based upon the average of these two amounts, \$614,516, which exceeds the AGI of the top 2% of taxpayers in 2002, SBA concluded Mr. Saldarriaga, the person upon whom eligibility is based, is not economically disadvantaged.

percentile of income earners, is not economically disadvantaged); *Matter of The Corvus Group, Inc.*, SBA No. BDP-184 (2002) (owners ineligible for 8(a) program because their AGI placed them in top two percent of all taxpayers); *Matter of Pride Technologies, Inc.*, SBA No. MSB-557 (1996) (applicant owner is not economically disadvantaged when his AGI exceeded that of ninety-nine percent of all U.S. individual taxpayers); *Matter of TAO of Systems Integration, Inc.*, SBA No. MSB-528 (1995) (applicant owner denied 8(a) program eligibility because his AGI placed him in top two percent of wage earners); *Matter of Super Solutions Corporation*, SBA No. MSB-461, at 16-17 (1994) (applicant owner's claim of economic disadvantage was unpersuasive when his income was in the top percentile of all taxpayers); *Matter of Autek Systems Corporation*, SBA No. MSB-417, *after remand*, SBA No. MSB-420 (1992), *aff'd sub nom. Autek Systems Corp. v. United States*, 835 F. Supp. 13, 15 (D.D.C. 1993), *aff'd*, 43 F.3d 712 (D.C. Cir. 1994) (per curiam) (unpublished opinion) (SBA does not need a specified percentile figure as a cutoff point in determining if applicant owner's income in the two years prior to application preclude a determination of being economically disadvantaged).

Petitioner attempted to rebut SBA's conclusion Mr. Saldarriaga is not economically disadvantaged in its reconsideration request. Petitioner presented that Mr. Saldarriaga's two-year AGI does not exceed the 2% threshold, \$284,424, cited by the SBA in its initial denial. Petitioner adopted SBA's general calculation and then excluded S corporation income and spousal income, and deducted taxes paid. In addition to the narrative explanation, Petitioner also provided the mathematical calculation specifically identifying the amounts subtracted for each year. Based on Petitioner's calculation, Mr. Saldarriaga's two-year average AGI for 2003 and 2004 is \$169,141.

In its reconsideration denial, the SBA acknowledged the evidence submitted by Petitioner to show Mr. Saldarriaga's income is not excessive. SBA adopted Petitioner's exclusions for S corporation income reinvested in the business and Petitioner's exclusion for income attributable to Mr. Saldarriaga's spouse. The SBA modified Petitioner's deduction for taxes paid on Petitioner's income. The SBA explained that although taxes paid on behalf of the business are reasonable, Mr. Saldarriaga's personal income taxes are not. SBA subtracted \$100,300 from Mr. Saldarriaga's 2003 AGI and \$76,200 from his 2004 AGI, as opposed to Petitioner's respective exclusions of \$186,242 and \$143,097.

SBA's reconsideration denial calculation deviates substantially from Petitioner's due to the addition of income reported on Petitioner's Schedule K-1. For the first time in the reconsideration denial SBA added \$150,000 to Mr. Saldarriaga's 2003 AGI and \$127,390 to his 2004 AGI. SBA does not explain why it deviates from the normal adherence to AGI. SBA's new process of editing an individual's AGI is problematic and strays from past practices and precedent.

Based on this calculation, in its reconsideration denial SBA reached a new conclusion: Mr. Saldarriaga's S corporation income reinvested in the business should be excluded, Mr. Saldarriaga's spouse's income should be excluded, taxes paid on Petitioner's income should be excluded, and Petitioner's K-1 distributions should be added. Thus, on reconsideration SBA used a new calculation to find Mr. Saldarriaga's two-year average is \$384,390 and he is not economically disadvantaged.

Rather than allowing Petitioner an opportunity to rebut SBA's new calculation, which for the first time accounted for Petitioner's K-1 distributions, SBA identified OHA as Petitioner's only recourse. This is contrary to the regulation. The regulation specifically states "If the AA/SDBCE declines the application solely on issues not raised in the initial decline, the applicant may request consideration as if it were an initial decline." 13 C.F.R. § 124.1008(f)(3)(ii). Although an applicant is not entitled to a second reconsideration if the denial on reconsideration is the same as one or more reasons addressed in the initial denial, *id.*, in Petitioner's initial denial the SBA did not consider, or even mention, Mr. Saldarriaga's S corporation income reinvested in the business, Mr. Saldarriaga's spouse's income, taxes paid on Petitioner's income, or Petitioner's K-1 distributions. Yet, on reconsideration these factors were relied on by SBA to find Mr. Saldarriaga is not economically disadvantaged.

Thus, rather than following the course envisioned by the regulation, Petitioner had no option but to proceed to OHA to challenge SBA's newest calculation. By limiting Petitioner's recourse, SBA strayed from the regulations and forced Petitioner to bypass the opportunity to resolve the controversy with the AAA/DPCE. Since the reconsideration request is the last opportunity an applicant for SDB certification, or recertification, has to present evidence to support its admission into the SDB program, Petitioner was unable to present additional evidence to the SBA to rebut this new conclusion and establish that Mr. Saldarriaga is economically disadvantaged.

With no other choice, Petitioner rebuts SBA's new calculation of Mr. Saldarriaga's two-year average AGI in its Appeal Petition to OHA. Petitioner argues there is no authority to add the K-1 distributions to Mr. Saldarriaga's AGI. Petitioner notes the sums added to Mr. Saldarriaga's income for 2003 and 2004 have previously been reported as income to the SBA for previous SDB certifications and, moreover, the sums have previously been reported to the IRS and taxed. Petitioner argues this results in the amounts being counted as income twice. In Petitioner's Reply to SBA's Response, Petitioner submits new evidence. This new evidence was not considered by the SBA and the new evidence cannot be considered in this appeal. 13 C.F.R. § 124.1008(f)(4)(ii).

Accordingly, Petitioner's Motion to file new evidence is DENIED, while its Motion for leave to correct errors in its Reply is GRANTED.

Regardless of the reason for SBA's conclusion that Mr. Saldarriaga is not economically disadvantaged, the new reason for denial requires the SBA to afford Petitioner the rights afforded on an initial denial. 13 C.F.R. § 124.1008(f)(3)(ii).

Neither part 124 nor part 134 provides a remedy for a failure by the SBA to afford an applicant an opportunity to address new matters the SBA raises when denying a request for reconsideration. I perceive two possible solutions: one solution is to consider SBA's failure to afford an applicant an opportunity to address new reasons arbitrary, capricious, or contrary to law, or, another solution is to remand the matter to SBA with instructions to adhere to 13 C.F.R. § 124.1008(f)(3)(ii), affording Petitioner an opportunity to respond to the new reasons and allowing SBA an opportunity to evaluate Petitioner's response. I choose the second option in this case because I believe it will afford the parties a fair determination.

There is considerable support preferring remand as a remedy for resolving this type of issue. *See, e.g., Matter of Encap Systems Corporation*, SBA No. MSB-515 (1995) (remanding to permit 8(a) applicant to address SBA's new reason for denial); *Matter of The Boston Group*, SBA No. MSB-487 (1994) (remanding to provide applicant an opportunity to rebut SBA's new reason for denial); *Matter of JTI Systems, Inc.*, SBA No. MSB-463 (1994) (remanding because applicant is entitled by regulation to reconsideration of the additional reason for denial); *Matter of Mega Analytical Research Services, Inc.*, SBA No. MSB-374 (1991) (remanding for a completion of the record since aspects of applicant's eligibility were not reconsidered); *cf.*,

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Matter of Paragon Systems, Inc., SBA No. MSB-440 (1993) (SBA raised a new reason on reconsideration, but further reconsideration would delay disposition and the matter could be resolved on facts in the record). These decisions support the rationale that until SBA makes a final determination concerning an applicant's ability to satisfy all of SBA's requirements for admission into an SBA program, the record is incomplete. A decision on whether it is arbitrary, capricious, or contrary to law is premature and would frustrate the intent of the regulations: to provide applicant businesses notice and an opportunity to respond to new conclusions of the SBA in reaching a final decision on an application.

III. CONCLUSION

The matter is REMANDED to the SBA for further consideration and a determination of Petitioner's eligibility consistent with this Decision and Order. The SBA shall follow the procedures mandated by 13 C.F.R. §124.1008(f)(3) requiring the SBA to treat the reconsideration denial based on new reasons as an initial denial and afford Petitioner all of the rights it received on the initial denial. The SBA may consider the evidence submitted in this appeal and determine if that evidence is sufficient to satisfy Petitioner's eligibility requirements or it may request additional material from Petitioner.

CHRISTOPHER HOLLEMAN
Administrative Judge